



Tax Information Bulletin

STATE BOARD
OF EQUALIZATION

ISSUED QUARTERLY
September 1996

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1. File on Time To Avoid Interest and Penalty Charges

Mailed returns must be postmarked by due date.

To avoid penalty and interest charges for late filing, your returns, forms, and payments must be postmarked on or before the specified due date. If you mail your return, please be sure to do so before the daily postal pickup to ensure a timely

postmark. Hand-delivered returns must reach Board offices on or before the due date.

If the due date falls on a Saturday, Sunday, or State holiday, returns postmarked on or received by the next business day will be considered timely.

If the return payment is due via electronic funds transfer (EFT), please refer to Pamphlet 80, *Electronic Funds Transfer Program Information Guide* for information regarding possible additional penalties (see also article 3).

2. Annual Taxpayers' Bill of Rights Hearing Scheduled

The 1996 Taxpayers' Bill of Rights Hearing will be held on Wednesday, November 20. At the hearing, individuals will have the opportunity to present recommendations to the Members of the Board regarding legislation, the quality of agency services, and other issues related to the Board's administration of its tax programs. The meeting will convene at 1:30 P.M. and will be held in the Board Room located on the first floor of Capitol Square, 450 N Street, Sacramento.

Although you do not need to be scheduled in advance to speak at the hearing, it would help us prepare if you contacted us beforehand to let us know what your topic will be. If your proposal is complex or extensive, we encourage you to submit it in advance and then summarize it in your oral presentation.

To notify us of a topic you wish to discuss or to send written material in advance, please contact:

Taxpayers' Rights Advocate Office
Board of Equalization
450 N Street MIC:70
P.O. Box 942879
Sacramento, CA 94279-0070
Telephone: 916-324-2798
Fax: 916-323-3319



3. Do You Pay Sales and Use Taxes Electronically?

How to avoid penalties.

If you are required to pay taxes by electronic funds transfer (EFT), there are certain conditions that must be met to avoid penalties. (These are explained in more detail in Pamphlet 80, *Electronic Funds Transfer Program Information Guide*.)

To avoid penalties, remember:

- Even though you may have made a timely payment of taxes, you must still file a timely return. It must be postmarked no later than the printed due date.
- If you use the Automated Clearing House (ACH) Debit method to transfer funds, your call must be completed prior to 3:00 P.M. Pacific time on the due date.
- Do not send your payment by any method other than by EFT (for example, do not use a check).
- If you report taxes on a prepayment basis, you are not required to file prepayment forms; however, you are still required to make EFT prepayments according to the prepayment schedule. (Taxpayers who do not pay by EFT are required to file prepayment forms.)

If you have questions regarding EFT payments, please call the EFT Helpline at 916-327-4229. Staff are available from 7:30 A.M. to 4:30 P.M., Monday through Friday, excluding holidays.

4. Uniform "Sale for Resale" Certificate Created for States Bordering Mexico

The four border states of Arizona, California, New Mexico, and Texas, together with the United Mexican States, have formed the Border States Caucus to create programs for promoting trade. One outcome of their discussions has been the creation of a uniform Border State "Sale for Resale" Certificate, which can be used by businesses

from the four U.S. states and from the northern border strip and border region of Mexico to buy goods for resale that will be transported across state and/or national borders.

How is the certificate used? A seller from northern Mexico or any of the four U.S. border states can submit a Border State "Sale for Resale" Certificate to purchase goods for resale. It is used in the same manner as a standard resale certificate.

Sales for resale are not subject to California sales tax; however, the seller of the goods must retain documentation to support the claimed exempt sale.

For sales made to merchants from the four U.S. border states, the seller can accept either a valid resale certificate or a valid Border State "Sale for Resale" Certificate. For sales made to merchants from the northern border region of Mexico, the seller can accept either a valid Mexican merchant resale certificate or a valid Border State "Sale for Resale" Certificate. A description of the Mexican merchant resale certificate is provided in Pamphlet 32, *Tax Tips for Sales to Purchasers from Mexico*.

Sales to Mexican merchants require additional documentation (see next column).

How can I obtain copies? Call the Information Center at 1-800-400-7115 for a copy of the Border States "Sale for Resale" Certificate. You can also request a copy of Regulation 1668, *Resale Certificates*, which explains what is required for a standard resale certificate.

Although the suggested format of the "sale for resale" certificate is considered to contain the essential elements of a resale certificate, the Board does not require its use. In fact, any document containing the essential elements of a resale certificate may suffice. As always, you should not accept resale certificates that are incomplete or inaccurate. You must ensure that all resale cards are signed at the time of accepting the card. An unsigned card is invalid.



Sales to Mexican merchants. If you make a sale for resale to a Mexican merchant, you are also required to obtain a copy of the merchant's official identification card or an imprint of the card on each sale invoice (this is in addition to obtaining a copy of the resale certificate).

Mexican merchants are authorized to purchase for resale only those items which would reasonably be sold by the type of business indicated by the code(s) on the card.

If you have any questions about the validity of an identification card or about the types of property a Mexican merchant can purchase for resale, you may call the San Diego office at (619) 525-4032. If you would like to receive a copy of the Pamphlet 32, *Tax Tips for Sales to Purchasers from Mexico*, please call the Information Center (see page 8).

5. Countering the Counterfeit

On occasion, taxpayers may unknowingly make cash payments to the Board using counterfeit currency. Because counterfeit money is not legal tender, the Board cannot credit the payor for the amount paid with such funds.

Currency used to make payment to the Board is routinely inspected. Any currency that is suspected to be counterfeit is sent to the United States Department of the Treasury. If the department determines that a bill is counterfeit, it will confiscate the bill and send a receipt to the Board. In turn, the Board will give the payor a copy of the receipt and advise them on how to resolve the payment shortage.

6. New Toll-Free Tax Evasion Hotline: 1-888-334-3300

Tax evasion affects all of us. It cheats hardworking, honest California citizens of millions of dollars of revenue for education and other important government services every year. To help address this problem and stop the underground economy from cheating us all, the Board has installed a

toll-free telephone number that concerned citizens can use to report suspected tax evasion.

Please call 1-888-334-3300 to report sales or use tax evasion or evasion of any of the other taxes and fees administered by the Board, such as fuel taxes, cigarette taxes, and alcoholic beverage taxes. Representatives are available to take your call from 8:00 A.M. to 5:00 P.M., Monday through Friday, except holidays.

7. Taxability of Sales Made by Humane Societies and Animal Shelters

Sales of nonfood animals in California are generally subject to sales tax. This includes sales made by humane societies, nonprofit animal welfare associations, and county or city operated animal shelters.

Nonfood animals include animals that do not ordinarily constitute food for human consumption, such as cats, dogs, burros, or hamsters. Sales of such animals are generally subject to tax even though the amount received may be designated as a "minimum donation," "adoption fee," or "placement fee."

As explained below, charges that are required as part of the sale are included in the amount subject to tax.

Spay/neuter deposits. If the customer is required to pay a fee for spay or neuter surgery prior to adopting an animal, that fee is subject to tax. If the fee is refunded once the customer provides evidence that the surgery was performed, the fee is no longer considered taxable and the tax initially collected must be refunded or paid to the state.

Required services. Similar to fees charged for spay and neuter deposits, payments for other services that are required prior to the adoption of an animal are also subject to tax. For example, fees for vaccinations, health examinations, deworming, disease testing, obedience training and microchip implants



would all be taxable if the owner cannot obtain the animal without paying for the services. However, if the services are optional (not required when adopting an animal), separately stated fees for the services would not be subject to tax.

Minimum donations. If the animal welfare organization charges a “minimum donation,” the taxable amount is the required donation amount. Separately stated amounts that exceed the required minimum are considered “true” donations. As such, they are not subject to tax.

For more information, please contact your local Board of Equalization office or call the Information Center (see page 8).

8. Application of Tax to Gift Wrapping Charges

With the holiday season rapidly approaching, it is important for businesses to understand the application of sales tax to gift wrapping charges.

Sales tax must be reported for the entire gift wrapping charge, including charges for labor and materials. It does not matter whether the gift wrapping is done by the seller or another party. The entire charge remains subject to tax.

If the person who does the gift wrapping is the seller of the contents, the gift wrapping is considered sold with the contents, whether or not a separate charge is made for the gift wrapping.

However, tax does not apply to charges for gift wrapping exempt food products sold by the person who does the gift wrapping, unless the value of the gift wrapping exceeds the value of the food products.

Persons performing gift wrapping may purchase wrapping material (such as paper, ribbon, tape, and so forth) for resale from suppliers of these materials.

9. Charges for Customizing “Canned” Computer Programs Can Be Taxable

Sales of prewritten (canned) computer programs are generally taxable, while sales of custom programs are generally nontaxable. However, if a client has a special need that requires the modification or customization of an available “canned” program, the charges for such customization may or may not be taxable.

Generally, if you charge your client for custom modifications to a canned program, those charges are nontaxable if they are separately stated on the sales invoice. If you do not state the modification charges separately, tax applies to the total charge for the program unless the modification is so significant that the resulting program qualifies as a custom program.

The modified canned program will be considered custom if the canned program was previously marketed and the price for the canned program is 50 percent or less than the charge for the new program. If the program was not previously marketed, the modified program will be considered custom if the charge for the custom programming modifications (as shown in the seller’s records) is more than 50 percent of the contract price for the new program.

As stated above, tax does not apply to the charge for a custom computer program. Charges for customizing canned programs and sales of custom programs can be claimed as nontaxable on your sales and use tax return on line 6 as nontaxable labor.

For more information on this subject, please call the Information Center and request a copy of Regulation 1502, *Computers, Programs, and Data Processing*.



10. Goods Delivered from Out of State May Be Subject to New Reporting Requirements

The following article does not apply to out-of-state retailers who are voluntarily registered to collect and report California use tax.—Editor

The method for allocating the 1% local use tax for certain sales and purchases changed July 1, 1996. The change, described below, applies only to *individual* sales or purchases of \$500,000 or more *when the goods are shipped from out-of-state inventories*. You may be affected by this change if (1) you are a retailer delivering goods to California customers from inventories located outside California or (2) you are a purchaser responsible for reporting the use tax on purchases delivered from out-of-state inventories.

Current Procedures

If goods are sold and delivered to a California customer from out-of-state inventories, the applicable tax is generally the use tax (as opposed to the sales tax). Retailers registered to collect the 1% local use tax generally allocate the tax based on the countywide area into which the goods are delivered. Such allocation is made on Schedule B and filed with the retailer's sales and use tax return.

If the out-of-state retailer is not registered to collect the use tax, the purchaser is generally obligated to report the tax on their own sales and use tax return. In cases where the goods are purchased for a location for which the purchaser does not have a separate permit, the 1% local use tax is generally allocated based on the countywide area into which the goods are delivered. Such allocation is made on Schedule B or Schedule E, when provided.

Procedures for Sales and Purchases Made on or after July 1, 1996

The local tax allocation procedures have changed concerning *individual* sales or purchases of \$500,000 or more *when the goods are shipped from out-of-state inventories*. In the past, the 1% local use tax for such

transactions was allocated based on the countywide area into which the goods were delivered. Now, the tax must be allocated to the specific jurisdiction (city or the unincorporated county area) where the first functional use will occur. (Functional use means the use for which the subject property was designed or intended.) Allocations for such sales or purchases must be made on Schedule F, *Detailed Allocation of 1% Uniform Sales and Use Tax*. (If you require a Schedule F and one is not provided with your return, please contact your local Board office.)

For individual sales or purchases of less than \$500,000, you may continue to allocate the 1% local use tax to the countywide area into which the goods are delivered.

For more information

Contact the Board's Local Revenue Allocation Section at 916-324-3000. Or call the Information Center (see page 8).

11. Local Tax Allocation Changes for Auctioneers

As of July 1, 1996, if you make taxable sales of \$500,000 or more at an auction event in a temporary location (a location that is not registered with the Board), you are required to allocate the 1% local tax for that auction event to the *city or unincorporated county area* where the auction (sale) takes place. Use Form BT-530-B, *Local Tax Allocation for Temporary Sales Locations and Certain Auctioneers*. If you need a copy of this form, please contact the Information Center (see page 8).

There is no change in allocation procedures for (1) auction events with taxable sales under \$500,000 or (2) auction events that are held at a location for which you hold a seller's permit. You will continue to allocate the local tax based on the specific address at which the sale occurred.



12. Common Errors Discovered in Audits: Property Used for Demonstration and Display

As a seller, if you use a resale certificate to purchase property for resale, you generally have no tax liability for the property until you sell it. However, if you take the property from your resale inventory and use it for a purpose other than for resale, you may be required to pay use tax for that use (for example, if you take the property and use it for personal purposes, that is a taxable use).

One use that is not normally subject to use tax is using property for demonstration and display purposes while it is held for sale in the regular course of business. For example, a retailer may take a vacuum from his or her resale inventory and use it for demonstration purposes before selling it. That use of the property is not subject to tax.

However, if the property is given as samples, it is not considered to be held for sale in the regular course of business and that use of the property is subject to tax, as explained below:

Example. A department store takes a bottle of perfume from its resale inventory and uses it for demonstration purposes as a tester at a perfume counter. Since the contents are being consumed (used), the tester bottle is not actually being held for sale. As a result, the department store must pay use tax based on the amount it paid for the bottle of perfume. (*Note:* This example assumes the store purchased the bottle without payment of sales or use tax.)

To report use tax, enter the amount you paid for the property under "Purchases Subject to Use Tax" on your sales and use tax return (line 2). The tax rate for use tax is the same as that for sales tax.

For more information about purchases that may be subject to use tax or about using resale inventory for demonstration and display, please refer to the December 1995

Tax Information Bulletin or call the Information Center (see page 8).

13. Donations from Your Resale Inventory to a Qualified Organization

If you purchase property for resale and subsequently remove it from your resale inventory and donate it to a qualified organization located in California, you are generally not liable for tax on the cost of the donated property. However, if you specifically purchase property for the purpose of donating it to the organization, your purchase is taxable and a resale certificate cannot be used (it is not a purchase for resale).

A qualified organization, according to Sales and Use Tax Regulation 1669, includes any organization described in Section 170 (b)(1)(A) of the Internal Revenue Code, including, but not limited to:

- Religious organizations such as synagogues or churches,
- Charitable organizations such as the Red Cross or Salvation Army,
- Nonprofit schools and hospitals,
- Medical assistance and research groups,
- Organizations operated for educational, scientific or literary purposes, including nonprofit museums, art galleries, and performing arts groups,
- Organizations operated for the protection of children and animals,
- Fraternal lodges, if the donated property is to be used for charitable purposes and not for benefit of the members, and
- The United States, California and any political subdivision of California.

If you have any questions or would like to obtain a copy of Regulation 1669, *Demonstration, Display and Use of Property Held for Resale*, please call the Information Center (see page 8).



14. Sales to the San Diego Violent Crime Task Force Are Exempt from Tax

The San Diego Violent Crime Task Force is a joint venture comprising various federal, state, and local law enforcement agencies. Because it is funded by federal monies and ownership of property acquired by the task force immediately passes to the United States Government, sales made to it are to be treated as exempt sales to the U.S. Government.

The San Diego Police Department is designated by the task force as its procurement agent. When making purchases, the department will issue an exemption certificate to the vendor. This certificate should describe the property being purchased and certify that it is being purchased for the task force, with title passing to the federal government before any use.

Certificates containing this information will relieve vendors from liability for the tax due on their sales to the task force. Accordingly, vendors are advised to retain a completed copy of this exemption certificate for their files.

For more information concerning the elements of a valid exemption certificate, please call the Information Center (see page 8).

15. Taxability of Membership Fees

Membership fees related to the anticipated retail sales of tangible personal property, are taxable when:

- The retailer sells its products only to members and the membership fee exceeds a nominal amount, or
- The retailer sells its products for a lower price to a person who has paid the membership fee than to a person who has not paid the fee, regardless of the amount of the fee.

Examples of membership fees that are considered to be related to the anticipated

retail sale of tangible personal property are membership fees charged by retailers such as PriceCostco or Sam's Club. When the membership fees for these organizations exceed a nominal amount, the fees are taxable. At this time, the Board recognizes "nominal amount" to mean an amount totaling \$40 or less per year.

Add-on charges (amounts received for memberships which are combined with the basic membership) are not considered part of the basic fee in determining whether or not the fee is nominal. Charges for additional cards issued under the same membership number are sales of separate memberships.

If the membership fee is not related to anticipated retail transactions, the fee is not taxable. For example, social organizations such as country clubs and other similar organizations are recognized as being essentially service organizations. Trade associations such as the California Association of Realtors (CAR) and Multiple Listing Service (MLS) are also considered to be primarily service organizations. Membership fees for service organizations are not related to anticipated retail transactions even though such organizations may incidentally sell tangible personal property.

For more information, please contact the Information Center (see page 8) and request a copy of Regulation 1584, *Membership Fees*.

16. Taxable Purchases Made from Out-of-State Retailers — Who Pays the Use Tax to the Board?

If you purchase merchandise from an out-of-state retailer and use the property for purposes other than for resale, the purchase is generally subject to use tax and must be reported. In some cases, an out-of-state retailer is registered to collect the use tax and will include it on the sales invoice. If you are given a receipt indicating you have paid the



California use tax to a registered out-of-state retailer, and the correct amount of tax was collected, you do not need to report the tax on your sales and use tax return.

However, if the out-of-state retailer does not include the California tax on the sales invoice, do not remit the tax with your payment to the retailer — even if the retailer is registered to collect the tax. If you do not have a receipt to prove that you have paid the applicable tax to a retailer who is registered to collect the tax, you remain responsible for reporting and paying the tax due on your purchase. (In most instances, a sales invoice that includes the correct amount of California tax and the seller's permit number will suffice as your receipt.)

17. Board Automates Several Compliance Functions

Improved identification of tax deficiencies anticipated.

The Board has recently implemented a system to automate its compliance functions. Called the Automated Compliance Management System, or ACMS, it will close the gap between accounts receivable and collections by reducing dependency on paper-based procedures. Because of its ability to capture collection information that was not previously available electronically, the system will make it easier for staff to identify and contact taxpayers who are delinquent in filing their tax returns or paying their taxes.

While the improved compliance and collection system will result in increased revenues, it will also contribute to the Board's mission of providing fair, firm, and uniform treatment of all taxpayers.

18. New and Revised Reference Materials

Sales and Use Tax Regulations

- 1525 Property Used in Manufacturing (Effective April 3, 1996)

- 1525.3 Manufacturing Equipment—Leases of Tangible Personal Property (Effective April 4, 1996)

- 1597 Property Transferred or Sold by Certain Nonprofit Organizations (Effective May 22, 1996)

- 1699 Permits (Effective May 24, 1996)

Revised Pamphlets

- 88 Underground Storage Tank Maintenance Fee (July 1996)
- 92 Alcoholic Beverage Tax (June 1996)
- 93 Cigarette and Tobacco Products Tax (June 1996)

For More Information

Information Center. Staff are available from 8:00 A.M. to 5:00 P.M., Monday through Friday, excluding State holidays. Call:

- 1-800-400-7115** (calls made in California)
- 1-916-324-2926** (calls from out of state)

For telephone devices for the deaf:

- 1-800-735-2929** (TDD phone)
- 1-800-735-2922** (voice phone)

Call 24 hours a day to use the automated fax-back service or to leave a recorded message requesting a specific publication.

Internet. Visit us at <http://www.boe.ca.gov> for information on sales and use tax rates by county, publications, district office telephone numbers, public meetings, and so forth.

Supply Unit. If you know the name of the publication, form, or regulation you need, you can write to the Supply Unit at 3920 West Capitol Avenue, Suite 200; West Sacramento, CA 95691. Or send a fax request to 916-372-6078.

Tax Evasion Hotline. If you believe a business should be reporting taxes and is not, you can call us toll-free to report it. Call during working hours at 1-888-334-3300.

Legislative Bills. Write to the Legislative Bill Room, State Capitol, Room B-32, Sacramento, CA 95814. The Bill Room does not provide copies of Board forms or publications.